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C O N F I D E N T I A L SECTION 01 OF 04 KUWAIT 000184

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STATE FOR NEA/ARP, EB, EAP
TREASURY FOR DAS AHMED SAEED AND JONATHAN ROSE
TREASURY PLEASE PASS TO FEDERAL RESERVE GOVERNOR KROSZNER

E.O. 12958: DECL: 02/05/2017
TAGS: [EAID](#) [ECON](#) [EFIN](#) [KU](#) [PREL](#)
SUBJECT: JOINT TREASURY-FEDERAL RESERVE DELEGATION MEETS
KUWAIT FINANCIAL SECTOR ELITE

REF: A. RIYADH 9103
[B](#). KUWAIT 4650
[C](#). KUWAIT 4115

Classified By: Acting DCM Tim Lenderking for Reasons 1.4 (b) and (d).

[1](#)1. (C/NF) Summary: On January 22-24, Department of Treasury Under Secretary for International Affairs Tim Adams and Federal Reserve System Governor Randall Kroszner met with leading Kuwaiti officials, financiers, and economists. The visit was the first for a sitting Federal Reserve Governor to the Gulf. Adams and Kroszner had excellent access to public and private financial sector elite including meetings with the Minister of Finance, the Governor of the Central Bank of Kuwait, the Director General of the Public Institute for Social Security, and more than twenty chairmen and general managers from Kuwait's top investment firms. GOK officials were skeptical about the GCC's 2010 monetary union target date and expressed misgivings about their decision to peg the Kuwaiti dinar to the dollar. GOK officials also described oil prices as unpredictable and stressed the importance of fiscal discipline in Kuwait, particularly among Parliamentarians. Numerous Kuwaiti interlocutors saw parliament as an obstacle to economic reform. End summary.

Joint Treasury-Federal Reserve Visit A Success

[1](#)2. (SBU) The first joint Treasury-Federal Reserve visit to Kuwait on January 22-24 strengthened dialogue, reinforced existing relationships, and established new ties. U/S Adams and Governor Kroszner were well-received by both GOK officials and the private sector. A January 23 lunch hosted by the American-Kuwait Alliance -- founded in September 2003 to facilitate the expansion of economic, political and cultural ties between the U.S. and Kuwait -- attracted chairmen and general managers from Kuwait's leading investment houses. The Deputy Governor of the Central Bank of Kuwait (CBK) also hosted a mixed public-private sector lunch for Governor Kroszner on January [1](#)24. Firms represented at the two events included: the National Bank of Kuwait, Kuwait Finance House, Gulf Investment Corporation, Citibank, the Commercial Bank of Kuwait, Boubyan Bank, Amwal Investment Company, Al-Ahlia Investment Company, International Financial Advisors, and more.

GCC Monetary Union: 2010 Target Unlikely

[1](#)3. (C/NF) During a January 23 meeting, Minister of Finance

Bader Al-Humaidhi reiterated Kuwait's commitment to the GCC's 2010 target date but noted that success "seems increasingly unlikely." CBK Governor Shaykh Salem Al-Sabah explained that the remaining time, is simply insufficient to make the requisite changes, legislative and otherwise, inside member countries. He predicts that like Oman (ref A) other GCC countries will soon realize that the target date is unrealistic. To assist the GCC in their efforts, Governor Kroszner offered to share information on the Federal Reserve System as a possible, although not exact, model for comparison. Al-Sabah agreed to share the offer with other GCC central bank governors during their next meeting in April 2007.

GCC Monetary Union: Kuwait Expresses Misgivings About Dollar Peg

14. (C/NF) Citing record high levels of inflation and concerns about the dollar's recent downturn, Minister of Finance Al-Humaidhi indicated that Kuwait is considering temporarily pegging the dinar to a basket of currencies if it appears that the ambitious 2010 target will be further delayed. When the GCC decided to embark on the formation of a monetary union, explained CBK Governor Al-Sabah, Kuwait was the only GCC country whose currency was pegged to a basket of currencies not the dollar. At the GCC's request, Kuwait pegged the dinar to the dollar.

Kuwait Oil Revenues Hard to Predict

15. (C/NF) Kuwait has a total aggregate budget deficit of 30 million KD. Ironical, Al-Humaidhi said, in a country with as

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much oil wealth as Kuwait. To balance the 2007 budget, he calculated an average oil price of \$45 USD per barrel. Three months ago with prices at \$68 USD per barrel this did not seem impossible. Today, with an ever-changing geopolitical climate and prices down to \$45 USD per barrel and falling, oil revenues are no longer guaranteed.

Private Sector Development and FDI Key to Kuwait's Economic Future

16. (C/NF) Al-Humaidhi noted that Kuwait's economic challenges are further exacerbated by shifting demographics -- over 60% of Kuwaitis are under 21. Twenty-five percent of Kuwait's 2007 budget is allocated to government salaries, most of which will be used to help the public sector absorb the latest influx of Kuwaiti graduates. To offset the trend, the GOK is encouraging new graduates to move into the private sector with a 200KD (USD 700) per month incentive. This is still less than the 500 KD average salary of GOK employees, explained Al-Humaidhi, and thereby actually saves the government money. The key to this strategy though is private sector development and foreign investment, which both Al-Humaidhi and Al-Sabah acknowledged is still lagging behind. "Foreign direct investment and a strong financial sector are vital to continued growth even in oil rich economies," said Al-Humaidhi, "but a shortage of labor and investors means that regional economies are in competition." In Kuwait, he conceded, outdated legislation and slow bureaucracy have led foreign and Kuwaiti investors alike to seek out more investor-friendly markets in Dubai and Bahrain.

Parliamentarians Impeding Progress

17. (C/NF) According to Al-Humaidhi, Kuwait's Parliamentarians have thus far rejected new, foreign investment-friendly legislation designed to promote privatization and reduce the taxation of foreign firms

despite continued lobbying by top GOK officials. The problem, he explained, is that Parliament is suspicious of GOK initiatives because of past mistakes. Meanwhile, pointing to a recent decision to give all Kuwaiti undergraduate students a 100KD (USD 350) stipend, Al-Humaidhi expressed frustration at Parliament's continued spending. Echoing Al-Humaidhi's concern about the lack of fiscal discipline, Governor Al-Sabah noted that as a three time chairman of the GOK's economic reform committee, he has yet to see tangible results. "We know what we need to do," he said, but getting legislation through Parliament has been difficult.

Foreign Banks in Kuwait

¶8. (C/NF) Governor Kroszner asked about the Central Bank about the role of foreign banks in Kuwait, and Econcouns raised the continued inequities in Central Bank regulations for Kuwaiti and foreign banks, citing the caps on loans for Citibank put in place by the Central Bank. Governor Al-Sabah insisted there is no unequal playing field in Kuwait and that "there is no problem" for foreign banks in Kuwait. He added that when foreign banks applied for licenses, they agreed to book credit in Kuwait. They have not done so but CBK has not pushed, he said. CBK Deputy Governor Nabeel Al-Mannae added that the Central Bank actually gave foreign banks preferential treatment for credit concentration. Al-Sabah did, however, note that he believes foreign banks should be allowed multiple branches - versus only one under the current law - and will raise this issue with Parliament.

Too many "leaders" in Kuwait

¶9. (C/NF) The delegation also met with Public Institute for Social Security (PIFSS) Director General Fahed Al-Rajaan. (Note: PIFSS administers Kuwait's pension fund which has approximately \$5 billion USD worth of investments in the U.S. End note.) Al-Rajaan reminisced about the youthful vigor and vision of the late Amir, Shaykh Jaber Al-Sabah, and noted that this is sadly lacking in today's leaders. "It is the individual that makes things happen," he said, concluding that the problem in Kuwait is management. "Shaykh Jaber used to make things happen," he explained, "but now we have too

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many leaders and everything is dragging." While he acknowledged that there are some extremely capable people in high-level positions, they do not work well together. There has been political deadlock in Kuwait for two years, he said, because there is simply too much democracy and no decision-making at the top. "Ministers can not execute plans because of Parliament, foreign tax and privatization reforms are still lagging" and, he added, the GOK will probably overturn the recent approval of 100KD stipends for college students. Al-Rajaan further noted that too much GOK interference in the private sector is creating an additional level of bureaucracy that is crippling the system.

Imminent Collapse of the Dollar Unfounded

¶10. (C/NF) Al-Rajaan dismissed media reports that regional investors are shunning dollar assets as mere "street talk." There has been no fundamental shift in investment strategies, he stated, and Kuwait still has about 50% of its investments in USD and 90% in the USD and G7 currencies. Al-Rajaan tied increased financial flows into Asia to increased surpluses in the global economy, not to the redirection of money out of the U.S. He added that Kuwait like the U.S. is investing in Asia, especially in countries like Vietnam that are behind the Asian development curve and where potential returns are greatest. Al-Rajaan cautioned that one risk that remains on the horizon is regional instability, in Iran as well as elsewhere due to Sunni/Shi'a tensions.

U.S. Economy: Forecast Good But Risk Remains

¶11. (C/NF) This visit was the first for a sitting Federal Reserve Governor to the Gulf and Kuwaiti interlocutors were keen to hear his "informal" assessment of the short-term U.S. economic outlook. Governor Al-Sabah, in particular, thanked Kroszner for his assessment noting that "growth in the U.S. is a reflection of world growth and with your assessment I feel more comfortable."

Chinese Economy: Hidden Dangers?

¶12. (C/NF) The Central Bank was eager to hear the delegation's assessment of China's economic outlook. Kroszner recognized China's impressive growth but expressed concern about market saturation and the banking system. If growth slows, he said, non-performing loans could become problematic because so many enterprises are state-sponsored. Adams cautioned that continued economic growth in China seems likely but migration, banking, and other challenges lie ahead -- perhaps not in the next 24 months but in the next 5-10 years. Deputy Central Bank Governor Al-Mannae concurred noting that "the risk for the global economy is the hidden problems in China." Al-Mannae added that China's economic growth has contributed to the slow down of inflation in Kuwait and any change in their currency would have a direct effect on the consumer price index in Kuwait. Al-Mannae described the current Chinese government as more cautious than the last and said he is waiting to see what happens at the end of the year when President Hu Jintao consolidates power.

Lebanon

¶13. (C/NF) When asked, Minister of Finance Al-Humaidhi reiterated GOK support for the government and people of Lebanon and mentioned Parliament's failure thus far to approve \$300 million pledged for Lebanon at the Stockholm conference in August 2006. The Minister said nevertheless that Kuwait would demonstrate support for Lebanon by participating in Paris III. Governor Kroszner also discussed aid to Lebanon with Arab Fund for Social and Economic Development Technical Director Ahmed Osman on January 24. Osman briefly listed AFSED grants to Lebanon to date (ref B, C) but voiced concern about Lebanon's absorptive capacity, especially in light of continued violence.

¶14. (U) This cable has been cleared by Treasury U/S Adams and Federal Reserve Governor Kroszner.

For more Embassy Kuwait reporting, see:

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<http://www.state.sgov.gov/p/nea/kuwait/index.cfm?cables>

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